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ECONOMIC REFORMS IN THE SOVIET UNION: A TRANSFORMATION TO THE MARKET

BY

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ECONOMIC REFORMS IN THE SOVIET UNION:
A TRANSFORMATION TO THE MARKET

AN INDIVIDUAL STUDY PROJECT

by

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ABSTRACT

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In August of 1990, the Soviet economy was in such bad shape that Mikhail Gorbachev sequestered his leading reform-minded economists to study and recommend a solution. Led by Stanislav Shatalin, these economists drafted the "500 Day Plan" detailing the necessary steps to transform the Soviet economy from a centrally planned to a market economy. Gorbachev initially endorsed this plan and the world-wide expectation and wonder was not whether the Soviet Union would transform its economy to a market economy, but when and how fast such a transformation should or could take place. This study will first present what the author believes to be the key components of a successful transformation to a market economy. Next, the study will examine the "500 Day Plan" or "Shatalin Plan" and compare and contrast it to the Council of Ministers' alternative reform proposal known as the "Ryzhkov Plan" recommended by Prime Minister Nikolai Ryzhkov. The study will then explore Mikhail Gorbachev's decisions as well as offer possible motives for these decisions. Finally, this study will conclude with some predictions about the future of the Soviet economy.

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CHAPTER I

Introduction

In the fall of 1989, when the Berlin Wall was demolished in Germany and statues of Lenin were torn down throughout Eastern Europe, few seemed to question what was being discarded. Similarly, few seemed to question what would take its place. The question which had not been sufficiently pondered was how to get from the crumbling wall and demolished statues to something resembling a smooth functioning and, most importantly, productive economy. For the Soviet Union, the seventy-plus year experiment with communism proved the system was painfully inefficient and wrought with problems. M. Welsey Shoemaker observes:

"The essential problem--and it is a continuing one--is that Soviet productivity slowed to a negligible rate in the 1960's and all the tinkering with the economy since that time did nothing to reverse that trend."¹

Talk of economic reform is nothing new for the Soviet Union. Even prior to Mikhail Gorbachev, many economic reform packages had been considered and attempted. However, it was Gorbachev who introduced ideas of glasnost and perestroika. Basically, glasnost means openness and perestroika means restructuring. To

a great extent, the glasnost begets the need for perestroika.

The openness to western economic and political ideas has resulted in some very different thinking in the Soviet Union. John Parker

comments:

"Perestroika, which began as a Dubcek-like policy of making socialism more efficient and humane, has become an attempt to turn the Soviet Union into a multi-party democracy and a free market...Mr. Gorbachev says that his main objective is to manage the transition from totalitarianism to liberal democracy without plunging the country into civil war."²

Stanislav Shatalin, a key economic advisor to Gorbachev,

adds:

"What this country needs to survive and to thrive is a new economic foundation, a new system. There is no escaping it."³

These comments seemed to reflect a dynamic mood in the Soviet Union and to portend forthcoming significant economic, political and social changes. The economic issue was not whether there would be a transformation to a market economy. The central economic question was how to successfully transform a centrally controlled command economy with the least amount of turmoil overall. Must you proceed slowly and spread the turmoil and pain of adjustment over a longer period of time? Should you make the

changes as rapidly as possible to pass through the tough adjustment period more rapidly? How much turmoil and for how long could the political system withstand? These are some of the issues and questions which are being considered at the time the author began this study.

During the course of the study, certain events have unfolded in the Soviet Union that have made these issues moot for the time being. Still, it is the author's opinion that these economic questions will one day be considered once again and therefore must be addressed.

SCOPE AND PURPOSE

The central purpose of this paper is to present a framework for market oriented economic reform in the Soviet Union. Specifically, the aim is to describe the essential economic factors necessary to transform the Soviet economy from a centrally-planned economy to a market-oriented economy.

The essential elements of such transformation are presented in Chapter II. While there are a countless number of elements, the limited scope of this paper dictates a discussion of only the essential factors. Chapter III is devoted to a description of the unique Soviet psychology. It is the author's opinion that any economic reform plan must take this unique psychology into account. Chapter IV first examines the two major and most recent economic plans under consideration. The chapter will continue with a description of the choices Mikhail Gorbachev has made. The final chapter offers an explanation of the reasons for Gorbachev's decisions and a prognosis for future economic change in the Soviet Union.

CHAPTER I

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1. Shoemaker, M. Weisley, The Soviet Union and Eastern Europe 1970, p. 47.
2. Parker, John, "The Soviet Union Massed Against the East," The Economist, 20 October 1990, p. 3.
3. Remnick, David, "Gorbachev Accepts Blame for Shortages," The Washington Post, 29 November 1990, p. A11.

CHAPTER II

Baseline Framework for Economic Transformation to a Market Economy

In this chapter, we will examine the most essential elements believed to be required for a successful transformation from a centrally directed command economy to a free market economy. The discussion is not intended to be all inclusive, and it is recognized there are other ancillary actions and reactions involved in such an economic transformation. However, the limited scope of this study dictates a discussion of only the essential elements.

In order to transform a centrally-planned state economy into a free market economy, five major conditions must exist in some form. In order of discussion, there must be private property rights, a system of free and flexible prices, financial reform to include international convertibility of the currency, and simultaneity. Finally, and most importantly, there must be a strong government in favor of the transformation and/or strong

support for the transformation among the vast majority of the populace. Let us examine each of these points individually.

The first key imperative for successful transformation to a market economy is the guarantee of the rights to private property. The very foundation of a free market system is private ownership of property, plant and capital. It is ownership and the right to reap the economic rewards (profits) of hard work that provides the incentive to take risk and work hard to achieve economic success. The entrepreneur must be guaranteed the fruits of his or her labor and risk-taking.¹

During a trip to his hometown this past summer, Mikhail Gorbachev encountered an old woman who spoke to the increased incentive of ownership. She said she looked after 50 cows on a collective farm but got almost nothing out of it. She suggested that she would make a far better living if she were allowed to own just two cows and sell their milk in a free market.²

In contrast, Hungarian Economist Jonas Kornai points out:

"The critical deficiency of socialist state property consists in the impersonalization of ownership: state property belongs to everyone and to no one."³

No one key individual assumes the risk of a new investment project with public ownership. The risk is spread to all and no one feels much of it as an individual. While one can imagine strict supervision and stiff penalties could be applied in a socialist state to achieve higher incentives to produce, such incentives come naturally without supervision with private ownership and committed individual risk-taking. It is private ownership together with the profit incentive that gives the free market system a built-in efficiency factor.

A second ingredient for a successful transformation to a market economy is a system of free prices. In a market system, price serves as the signal of what to produce, how to produce it (what resources to use), and as to who gets what (distribution). In simple terms, higher retail prices (caused by consumer demand, for example) for a certain product will cause (signal) producers to produce more of that product in pursuit of the higher profits. The higher profits will attract (signal) more producers (assuming free entry) to produce the product until the increased supply

reduces the price to an equilibrium level and reduces the profit level back to a normal level.⁴

Similarly, it is the relative price of raw materials and combinations of capital and labor that determine the most efficient and most profitable way to produce a given product.

Charles E. Lindblom in Politics and Markets comments:

"Market incentives are powerful. Indian peasants, for example, whose social isolation might be expected to render them impervious to market incentives, have repeatedly demonstrated their sensitivity to them by shifting from one crop to another as relative prices change."⁵

Without a system of flexible and free prices, economic signals are distorted. Prices too high cause surpluses and prices too low cause shortages. As a case in point, prices for most basic foodstuffs are held artificially low in the Soviet Union. The result has been constant shortages. Rather than price dictating who gets what in the Soviet Union, the person willing to stand in line the longest or push to the front the hardest gets the bread.⁶ "Price distortions produce large trade distortions (that is large deviations from the pattern of trade that would prevail if goods were sold at world market prices)."⁷

The third major ingredient for a successful transformation is financial reform to include an internationally convertible currency. The central bank will have to freely exchange foreign currency for the ruble. Only then will the ruble establish a true market value. In the Soviet case, this adjustment will certainly spell a devaluation in the value of the ruble. However, once the market rate is determined, it is then possible to achieve meaningful trade with other nations. On this point, academician O. Bogomulav adds, "Recognition of the importance of the market under socialism will remain empty words without real, solid money that serves as a real, not conditional purchasing means."⁹

Trade with other countries implies competition for sellers.

As a free market advocate, Janos Kornai argues:

"The competition in turn is one of the strongest incentives to ensure that the general public is better supplied, shortages eliminated and technical standards are developed."¹⁰

The fourth major requisite for a successful transformation to a market economy is simultaneity. All of these major actions

discussed, as well as others which could not be discussed due to the length of this paper, must be taken at the same time. All of the initiatives will have interconnected second and third order ripple effects. For example, a private entrepreneur deciding what new venture to pursue will certainly be impacted by foreign competition brought on by a legitimate exchange rate. Indeed, the increased international trade will offer many new opportunities for these new profit-seeking entrepreneurs. If simultaneity is not achieved, distorted signals will continue to be sent to decision makers (buyers, sellers, producers, workers, et al). Distorted signals and resulting miscalculations and bad decisions spell further disruptive adjustments in the future. Jonas Kornai put it this way, "The sum total of ten different kinds of half-results is not five full successes but five full fiascos."¹⁰

The final and most essential element of a successful transformation is government and/or popular support. The transformation to a free market economy will involve winners and

losers. While the winners will outnumber the losers, (otherwise the transformation should be discarded), the fact that there will be losers implies dissension, instability, and perhaps, conflict. Obvious losers are those workers from inefficient firms and factories, which will close as a result of the transformation. Another group are those living at the margin of poverty now who will drop below the line--at least initially--with expected higher prices. Still another group are those who disagree with wealth accumulation and significant differences in standards of living among individuals. All these groups and more could be the source of instability during the transformation.

Only a strong government can implement an economic policy of transformation to a market economy. As Janos Kornai says,

"Of course there are various kinds of 'strong governments.' A stabilization program accompanied by a great upheaval and a reinforcement of the market economy might be carried out by a responsive, authoritarian administration, a military dictatorship of the Chilean or Turkish variety...the other possibility is a government whose strength lies in the support of the people, one to which free elections have given a real popular mandate to set the economy right with a firm hand."¹¹

Whatever the form of government, social concern is a key ingredient to successful transformation. Dr. Jeanine

Braithwaite, Economist for the Center of International Research, U.S. Bureau of the Census, argues that strong leadership can help secure the necessary popular support.¹²

Many would-be reformers in the Soviet Union have recognized the importance of popular support and have "...complained: the reason our government cannot introduce a reform programme like Poland's is that we do not have the support of a Solidarity..."¹³ In fact, "Only after the Polish people elected a government in which they had confidence did a free-market revolution become possible."¹⁴

The reader should keep these key and essential elements for a successful transformation to a market economy in mind as we explore the Soviet reform proposals and actions taken in the following chapters.

CHAPTER II

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4. By normal level, I mean the rate of return which entrepreneurs feel is appropriate for the level of risk and a level which will not cause entry or exit from the industry in question.
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7. "The Soviet Union, Massed Against the Past," The Economist, 20 October 1990, p. 10.
8. Yanowitch, Murrey, "Economist-Deputies on Radical Economic Reform," The Soviet Review, September 1990, p.6.
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11. Kornai, Janos pp. 118 & 119.
12. Braithwaite, Jeanine.
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14. Dobbs, Michael, "Gorbachev's Dilemma a Familiar One," The Washington Post, 22 October 1990, p. A19.

CHAPTER III

The Soviet Psychology

In theory, a free market system should work to efficiently allocate society's scarce resources just as Adam Smith advocated. At the nucleus of this free market system is "rational man" who makes decisions which are optimal for himself and designed to propel himself ahead. Fortunately, for society as a whole, "rational man's" success results in society's benefit. On the one hand, society's welfare is mainly the sum of individual welfare. More importantly, "rational man" can improve his economic position in a free market only by producing or providing something society places value on and is thus willing to pay for.

Unfortunately, the "rational man" theory may not hold up in the Soviet Union. In fact, the social psychology in the Soviet Union is so different from the west and may play such a critical, as well as detrimental, role in any economic reform that this entire chapter is devoted to its description and possible impact.

In general, the key characteristics of the Soviet

psychology, which could impact adversely on attempts to reform the Soviet economy, are their apathy towards work, their dependence on the state, their escapism, their vicious envy of people who have more of something and their overall lack of entrepreneurial skills.

First, the Soviet people, in general, are lacking in terms of a strong work ethic.

Hedrick Smith comments:

"If America is dominated by workaholic 'Type A's,' the Soviet Union is mired in hard-to-motivate 'Type B's.'" ¹

This lack of motivation on the part of workers in the Soviet Union is well recognized by the Soviets. Abel Aganbegyan, chief economic advisor to Mikhail Gorbachev, in his book, Inside Perestroika, the Future of the Soviet Economy, says, "the central problem of the new economic system: (is) how to make people care about the results of their work, how to initiate, as part of the economic reform, feelings of personal responsibility."²

Second, the Soviets have a "cradle-to-grave" mentality. That is, they are extremely dependent on the state for guidance,

initiative, for survival. A Soviet would typically ask what the state can do for him rather than what he can do for himself.

This dependence on the state dates back prior to Socialism, probably as far back as the days of Serfdom.³

Regardless of its historical roots, Hedrick Smith notes that this dependency on others begins at childhood:

"Russians are soft on their children, spoiling them, trying to protect them from hardship; they keep them living at home after university and often support them financially during those years. The contrast with American young people is so striking that Soviet writers and journalists, reporting on travels across America, have been moved to send home detailed descriptions of the summer jobs taken by American college students."⁴

With respect to lifelong dependency, Hedrick Smith adds:

"Dependence on parents is a prelude to dependence on the state, which the Soviet system encourages. After graduation, university students are assigned jobs under *raspredeleniye*--literally, the "distribution"--which they must accept as a way of paying back to the state for their education...The individual fits into the local hierarchy, which both supports him and checks his initiative...Dependence is also nurtured by subsidies for the essentials of living--housing, food, health care, education."⁵

A third general characteristic of Soviet psychology is escapism. On the one hand, life has been so harsh for so long for the average Soviet citizen that he or she can endure much hardship before complaining.

On the other hand, Soviets do not like to admit things are as bad as they are.

Hedrick Smith notes:

"In this view, Russians are prone to escapism, whether it be the 'lazy, dreamy' philosophizing of the intelligentsia, as Tolstoy put it, or the brutal, often self-destructive mass alcoholism of workers and peasants...The system itself not only encourages but nourishes, such behavior. The grim shortage of goods sends Russians seeking instant gratification. Why, if the future offers little hope, plan for the long term? Why not blow a month's salary on a birthday party?...Russians are not a career-driven people; their primary touchstones are not success, getting ahead, making deals, accumulating material possessions."*

A fourth characteristic, and the one which could most adversely affect attempts at economic reform, is Soviet envy and abhorrence of unequal success. The Soviets have a deep mistrust of anyone who is successful or who has more of something. The Soviets believe in more than just equal opportunity. They believe there should be an equal outcome for all. Felicity Boninger, a former New York Times correspondent in Moscow, once made the observation that "in America, it's a sin to be a loser, but if there's one sin in Soviet society, it's being a winner."?

Anatoly A. Sobchak, the mayor of Leningrad, once commented:

"Our people cannot endure seeing someone else earn more than they do. Our people want equal distribution of money, whether that means wealth or poverty. They are so jealous of other people that they want others to be worse off, if need be, to keep things equal."⁹

A fifth characteristic standing in the way of economic transformation is really the lack of needed trait or ability.

The Soviets have a disparity of folks with entrepreneurial experience or spirit. In commenting on this shortcoming, the 15 December 1990 issue of The Economist notes:

"(A key question mark is) whether the Russians can spot and exploit potential markets, entrepreneurial skills for which they are not famous."⁹

It turns out the Soviets have had very little practical experience at entrepreneurship for over 70 years. However, this concern may not be valid below the surface of general economic activity. On one hand, in the agricultural sector, small private plot owners have been extremely productive. Certainly those skills could be successfully transferred to larger ownership plots that might become available and legal under economic reform. In addition, an extensive black market economy exists in

the Soviet Union. No one knows how large the black market is, but these skills would certainly become useful once legalized under the rubric of market reform. The point is that, while the Soviet Union does have a shortage of entrepreneurial skills, this shortage may not be as acute as might appear on first examination. The real question may be how to unleash and redirect these entrepreneurial skills.

In summary, any attempt to transform the Soviet economy to a free market system must take into account these Soviet traits. Mikhail Gorbachev is fully aware that he must consider these special characteristics. Soviet Economist Anatoli Strelyani notes that Gorbachev "deplores the well known character traits of his countrymen--to obey order unquestioningly, to shun responsibility or risks, to put up meekly with hardships."¹⁰

CHAPTER III

ENDNOTES

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3. Twining, David I., Lecture, U.S. Army War college, 23 January 1991.
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7. Ibid, p. 71.
8. Ibid.
9. "Converting Soviet Arms Factories," The Economist, 15 December 1990, p. 21.
10. Remnick, David, "Gorbachev Shifts on Economy," The Washington Post, 13 September 1990, p. A31.

CHAPTER IV

Gorbachev's Economic Choices and Decisions

In this chapter we will first examine the essential components of the two most seriously and recently considered economic reform plans in the Soviet Union. We will then describe and evaluate the choices Mikhail Gorbachev has made. The first plan is the more radical 500-day Shatalin Plan recommended by Economist Stanislov Shatalin. The second plan is a more conservative plan set forth by Prime Minister Nikolai Ryzhkov and the council of ministers.

The Shatalin 500-day plan unequivocally endorses the free market. The plan begins with the words:

"Humanity has not yet developed anything more efficient than a market economy...The prerequisite to ensure the effective functioning of the market includes de jure equality of all types of property, including private property...Revenue from property should be recognised as lawful profit."¹

The plan calls for a loose federation of sovereign republics bound by a system of bilateral economic pacts. The republics retain full control over their resources. Central planning is abolished along with most union economic ministries. The Union

budget deficit would be reduced by immediate and radical budget cuts focused mainly on the army, R&D and industrial construction projects. The plan also advocates sales of state property to achieve as high as 70% private ownership of enterprises and some unknown high percentage of individual form of ownership. In addition, the Shatalin plan urges rapid movement toward a free price structure with some temporary exceptions granted for essentials.² The Shatalin plan also calls for a stock market and other institutions found in western economies.³ Culturally, the Shatalin plan stresses economic freedom, entrepreneurship, free market spontaneity, and accepts the resultant economic inequalities.⁴ "The best known feature of the Shatalin plan details the order in which its reforms are to be introduced. This is the '500-day programme,' which provides what is virtually a day-by-day timetable. The Shatalin timetable itself, however, should not be taken literally. It is more a public commitment to practical action than a detailed schedule for economic reform."⁵ The plan appeals to youth and the educated classes.

In contrast, the Ryzhkov plan retains the Union government at the pinnacle of a politically tightly bound Union with control of energy resources, transport, communication, price, wage and other macroeconomic policies remaining with the central government. While the central government continues to operate these strategic state functions, the civilian ministries' (consumer goods) industrial property is turned over to enterprises and trusts. The central government retains only a coordinating role in the latter. Thus, there is decentralization of control with respect to the production of consumer goods. However, the Ryzhkov plan is biased toward the military sector, central controls, and massive capital projects rather than consumer goods. The Ryzhkov plan demands a referendum on private ownership of land. There is emphasis on joint stock companies with strong state participation in industry. In addition, the plan recommends collective and state forums. Prices continue to be regulated and accompanied by indexing of wages and subsidies. The cultural aspects embodied in the plan are the continuous need

for state regulation, and social guarantee (leading to grave concepts) and the traditional emphasis on Soviet and Russian state interests. There is a special concern for order. The plan appeals to older, less skilled workers and state employees.*

It appears on the surface that Gorbachev has thus far decided on a compromise between these two plans. However, a closer examination reveals a rejection of the Shatalin plan on the key issues. Let us here explore Gorbachev's choices. In the final chapter we will attempt to explain why he made those choices.

Initially, Gorbachev backed the 500-day Shatalin plan.⁷ In fact, many, if not most, Soviet analysts were surprised and shocked at Gorbachev's apparent rejection of central planning in favor of the free market. Gorbachev even appeared to recognize the importance of strong governmental backing and leadership of such a drastic change. M. Welsey Shoemaker points out:

"The General Secretary has thus been waging a propaganda campaign to convince the Soviet people that major economic reforms are necessary."⁸

Unfortunately, shortly after the public endorsement of the

Shatalin plan, right wing pressure from the army, KGB and government bureaucrats forced Gorbachev to seek compromise. For one bone of contention, none of these groups looked upon the proposed drastic budget cuts in their arenas favorably. As Mary Dejevsky observes:

"Mr. Gorbachev appears to have heeded critics within the government and gone back on his original preference for the 'dash to the market' advocated by his economic advisor Stanislov Shatalin."⁹

Michael Dobbs attributes the shift to Gorbachev's wavering back and forth indecisiveness:

"Over the past year, he has appeared to veer from one to the other, hoping to avoid the fateful moment of decision. One day, he appears on the verge of forming a political alliance with his principal rival, Boris Yeltsin, president of the Russian republic. A few days later, he is raising the specter of 'emergency measures' in selected parts of the country to cope with unrest."¹⁰

M. Welsey Shoemaker adds:

"Gorbachev's greatest problem is, and has been, that while the top leadership favors reform, the working level bureaucrats who have to implement any reform remained unconvinced, particularly when it might involve loss of their jobs."¹¹ While "everyone in the top leadership accepts the necessity of economic reform...several want the reform to be as narrow and technical as possible."¹²

Let us examine some of the specifics of Gorbachev's choices in terms of the necessary framework for economic reform as set

forth in Chapter II. On the issue of private property rights, Gorbachev chose not to endorse private property rights. Instead, he decided to put this controversial issue to a referendum which has not been scheduled as of this writing. While there has been much debate and discussion of prices and inflation, there has been no talk of free prices. Monetary reform to achieve stabilization has been attempted via confiscation measures. One such measure was a plan to declare large banknotes (50 and 100 ruble notes) as no longer legal tender after midnight, 23 January 1991. "A presidential decree restricted the right of exchange in most cases to one month's salary."¹³

This monetary reform measure was reportedly directed at black marketeers. However, Michael Dobbs reports:

"The primary purpose of Gorbachev's decree was to restore balance to the consumer market and shore up the purchasing power of the ruble by soaking up the excess money now in circulation. Over the past three years, the state of mind has been pumping out bank notes unmatched by food or consumer goods. As a result, stores throughout the Soviet Union have been cleaned out."¹⁴

By solving the excess ruble problem in this draconian fashion, Gorbachev has signaled the complete abandonment of any

immediate plan to embrace the free market. Had he been serious about the free market, he could have more than absorbed the excess rubles by selling off state property as advocated by the Shatalin plan. As an alternative, merely freeing prices and letting them rise would have absorbed excess rubles. The higher prices would have stimulated supply (production) in the longer run in a free market environment. The immediate result of this confiscation policy is the ruble remains and will likely continue to remain nonconvertible on the international exchange market. As addressed in Chapter II, this lack of convertibility stands as a major hinderance to much needed international trade.

In summary, Gorbachev has taken little, if any, positive action on the measures described in Chapter II as necessary to transform the Soviet economy into a free market economy. "After weeks of hesitation, Gorbachev evidently concluded that he could not risk such a leap into the unknown."¹⁵

Having abandoned the dash to the free market, Gorbachev now seeks reform partly in terms of conversion of Soviet defense

factories to produce consumer goods. However, as the 15 December 1989 issue of The Economist points out, "Soviet consumer goods and managers will improve in quality and number not when defense bureaucrats are replaced by civil ones, but when they are forced to improve by market competition."¹⁴

In the next chapter, we will examine why Gorbachev made these choices.

CHAPTER IV

ENDNOTES

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CHAPTER V

Conclusion and Prognosis

When the research for this study began, the Soviet leadership was pondering the question of not whether but how fast and how far they should move toward a free market economy. Unfortunately, recent events indicate that these decisions have been pushed aside for the time being. The overall political instability of the Soviet Union has overshadowed the debate on economic reform.

The irony of the current political instability is that it likely resulted in a large part from the failure to act progressively on the economic reform issues. In August of 1990,

M. Welsey Shoemaker warned:

It is unlikely Gorbachev will be successful on any of his political reforms "unless he is able to carry through his economic reforms quickly and to demonstrate that they will actually make life better for everybody. Unfortunately, it is in precisely this area that he has shown the least amount of vision."¹

The Soviet Union today is in a state of political and economic turmoil. Several republics have sought independence and

many others want less control from the central government. In order to make it through the winter, the Soviets have requested and received massive food aid from the west. The 500-day Shatalin plan was discarded, and despite all the talk about glasnost and perestroika, the Soviet Union is still a centrally-planned economy. Basic patterns of ownership remain essentially the same. The central ministries continue to run 80% of the companies. There are no markets for land, labor and capital, and prices are still set by government fiat.²

Gorbachev's compromise plan is under attack from both left and right. While right wing conservative legislators criticize him for failure to take decisive action against separatists and to prevent ethnic strife, radical reformers say even harsher measures are needed now that Gorbachev has delayed taking any material reform action.³

As a result of the failure of the central government to act decisively, many of the republics have decided to go it alone both politically as well as economically. Pockets of free market

experiments exist throughout the Soviet Union.

The problem is that, all over the country, enthusiastic free marketers are putting their ideas into practice in the only place they can--their region--while using the insidious instrument of rationing to defend otherwise sensible policies. Leningrad, for example, is one of a dozen cities hoping to set itself up as a free economy zone. Its admirably free marketing deputy mayor, Mr. Anatoly Chubais, wants to start by taking all the factories in the city under the wing of the local council, presumably as a first step towards the introduction of genuine free market policies. But how do you isolate Leningrad from the surrounding economy which uses the same currency?"

Perhaps the primary reason Gorbachev rejected the 500-day program urged by his and Boris Yeltsin's economic advisors is that he recognised the remedy it implies is the decentralization of power in the Soviet Union. For a multinational empire like the Soviet Union, decentralization is the equivalent of dismantling that empire.² Pure and simple, the circles of power in the KGB, the army and the communist party faithfuls, would not stand by and watch the dismantling of the Soviet Union.

So, like Poland in 1981, the Soviets have shifted back to the right. Will the Soviets ever see democracy and, for the purpose of this study, a free market? Was Chapter II of this study, the framework for successful transformation to a market

economy, written in vain?

The silver lining to this dark cloud is the possibility that true and thorough economic reform might someday be successfully pursued. "The Soviet Union has not yet proved that economic reform cannot work."

In this author's opinion, the economic and political freedom experienced thus far in the Soviet Union will preclude a complete reversal. The Soviets are clamping down politically and economically. However, once political stability is achieved, the Soviet Union will be forced to develop a more productive economic system, perhaps something that resembles very closely the free market economic system. While the new system may resemble the free market system, it will be uniquely Soviet. Its development will certainly reflect the unique Soviet psychology described earlier. Even the pace of the transformation will most likely be influenced by the almost eternal Soviet patience for suffering.⁷ This current crackdown and shift to the right is but a step backward to be followed by two or more steps forward in

the future. Mikhail Gorbachev must be given the credit for the beginning of the reform movement via his Glasnost policy. However, he has failed miserably at Perestroika. In this author's opinion, he missed his window of opportunity when he abandoned the Shatalin plan in September 1990. It is unlikely Gorbachev will survive the next round of reform attempts. And there will be reforms in the future. As the widow of Andrei Sakharov, Elena Bonner, says in reference to possible reversal:

"No... Things have gone too far."e

CHAPTER IV

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